

Role of Investment Consultants: Private Asset Classes

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Background

- Board has raised questions regarding multiple roles of some CalPERS investment consultants
 - Board Consultant
 - Independent Fiduciary for Real Estate Investment Decisions
 - Special Projects for Staff

Today's Agenda

- Outline current roles of the private asset class investment consultants
- Discuss key questions regarding consultant roles and a potential model
- Solicit feedback from the Investment Policy Subcommittee in order to develop final recommendations

Current Board Consultant Role: Private Asset Classes

Strategy & Policy Analysis	<ul style="list-style-type: none">• Provide high level strategic advice• Review policies/guidelines and make modification recommendations• Review strategic/annual plans• Identify and report on investment opportunities
General Investment Analysis & Research	<ul style="list-style-type: none">• Provide independent review, analysis, and opinions with respect to new opportunities• Provide analysis of market developments• Validate accuracy of incentive fee calculations and structures for investment partners
Performance Analysis & Monitoring	<ul style="list-style-type: none">• Prepare investment performance reports and portfolio analysis• Provide guidance on performance methodologies• Advise on program implementation (when appropriate)• Recommend indexes to benchmark (when appropriate)
Independent Advisor to the IC	<ul style="list-style-type: none">• Provide independent review and analysis on opportunities• Provide independent risk reports and analysis of programs• Advise the IC on aspects of the program and its implementation

**Duties per Contract No. 2009-5105, LOE #RE-5 and Contract No. 2009-5106*

Current Consultant / Staff Framework – Investment Decisions


	AIM*			Real Estate*		
	Board Consultant	Spring-Fed Pool Consultant	Staff	Board Consultant	Spring-Fed Pool Consultant	Staff
Transaction is under Delegation of Authority limits	✓ Provides memo stating the transaction complies with policy and delegation	✓ Provides <i>Prudent Person Opinion**</i> to Staff	✓ Analyzes transaction and makes investment decision	✓ Participates in transaction discussion and provides opinion on transaction to the IRC***	✓ Provides <i>Independent Fiduciary Recommendation**</i> to Staff	✓ Analyzes transaction and makes investment decision
Transaction is above Delegation of Authority limits	✓ Provides opinion on transaction to the IC	✓ Provides <i>Prudent Person Opinion**</i> to Staff	✓ Analyzes transaction and provides recommendation to the IC	✓ Provides opinion on transaction to the IC	✓ Provides <i>Independent Fiduciary Recommendation**</i> to Staff	✓ Analyzes transaction and provides recommendation to the IC

* The illiquid assets within the Inflation Linked Asset Class portfolio (i.e., Infrastructure and Forestland) use a different investment decision making model. When an investment decision making model is approved, staff will conform the decision making process for these assets to the approved model.

** See Appendix for proposed definition of Prudent Person Opinion and Independent Fiduciary Recommendation.

*** The role of the Investment Review Committee (IRC) is to review all real estate investment decisions and provide a recommendation to the Senior Investment Officer, Real Estate.

Current Consultant Fees: Private Asset Classes

	AIM		Real Estate		
	Board Consultant	Spring-Fed Pool Consultant	Board Consultant	Spring-Fed Pool Consultant	PCA (Spring Fed Pool)
Annual Board Consultant Fees	\$495,000	\$0	\$1,083,000	\$0	\$0
Spring-Fed Pool Consultant Fees (FY 2009-10)	\$0	\$6,446,436	\$0	\$6,000,000	\$2,642,550
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					<div> <p>LOEs Related to Independent Fiduciary Duties Total: \$1,414,500</p> <p>LOEs Related to Other Projects for Staff Total: \$1,228,050</p> </div>
Consultants	PCA	Various Top 3: LP Capital, Credit Suisse, and Hamilton Lane	PCA	Various Top 3: PCA, Bard Consulting LLC, and Le Plastrier Development Consulting	

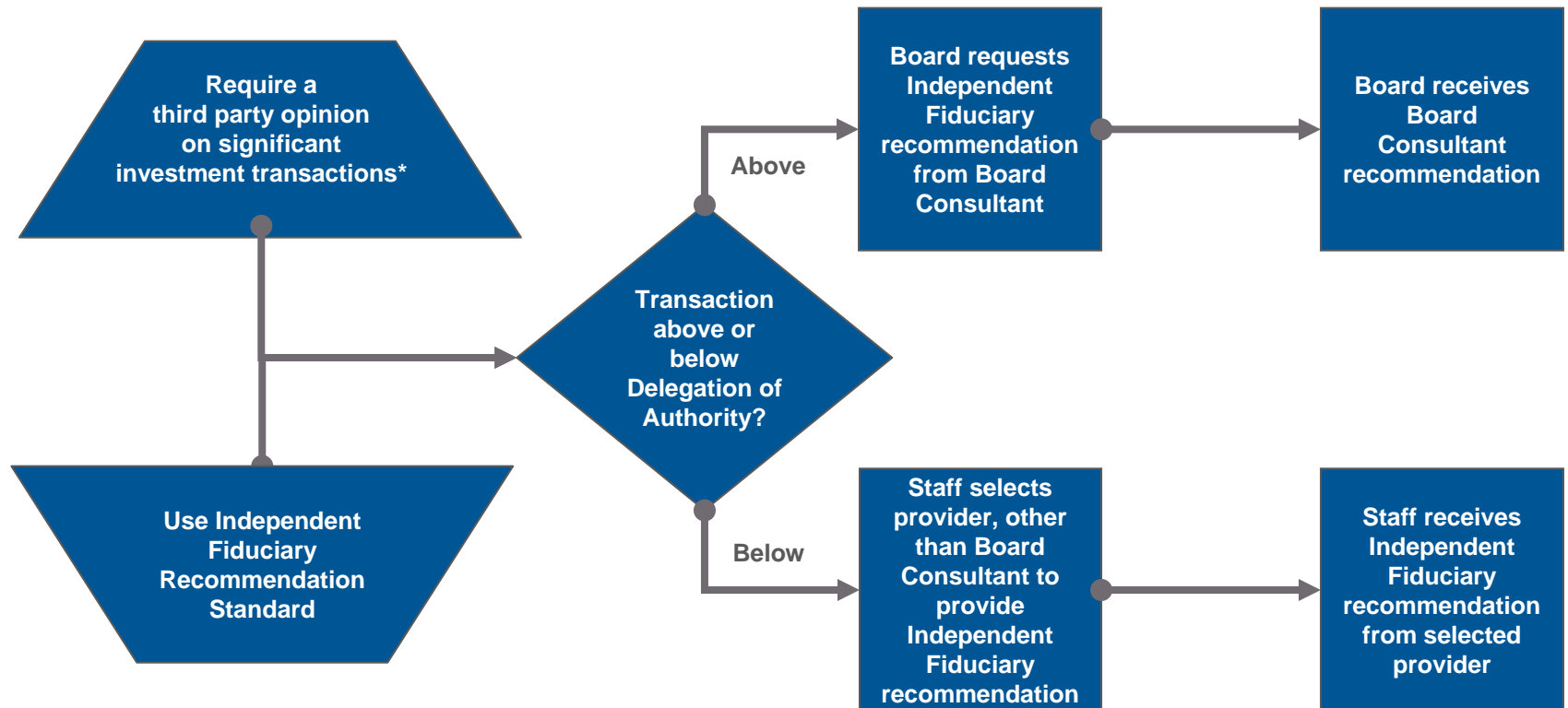
History of Real Estate Consultants

- Pre-2007 Role
 - Real Estate Staff had discretion in making investment decisions
 - SIO had authority to make investment decisions, in most cases, without third party review
- Rationale for change
 - In 2005 and 2006, at the height of the real estate market, the Real Estate Unit made more than \$27 billion in commitments, most of which were made under delegated authority
 - In most cases, neither the Investment Committee nor the Board Consultant was involved in the decision-making process
- Current Role
 - Independent Fiduciary Recommendation required for Real Estate investment transactions above 2.5% of the Real Estate Policy Target Amount
 - Deliberate policy decision by the Investment Committee to require Board Consultant to be the Independent Fiduciary for all major investment decisions
 - The Board Consultant is required to participate in the Real Estate Division's Investment Review Committee (IRC) for all investment decisions, regardless of size

Key Questions

- Do we need a third party opinion on significant investment decisions?
- What is the standard for the third party opinion - Independent Fiduciary recommendation or Prudent Person opinion?
- Who is the third party opinion provided to – Board or Staff?
- Who hires the provider of third party opinion – Board or Staff?
- Is the third party opinion part of the Board Consultant role?
- Can Board Consultant provide additional, specific consulting services to Staff via a spring fed pool?

Potential Model: Private Asset Classes



Guiding Principle:

Board Consultant cannot perform work for Staff as an Independent Fiduciary or on special projects.

* Significant investment transactions to be defined.

Next Steps

- Staff to finalize proposal for Policy Subcommittee consideration
- Policy Subcommittee to agree on proposed model for further discussion with Investment Committee
- If existing model changes, agree on transition period for Real Estate regarding use of PCA

Appendix

Proposed Definitions

- Prudent Person Opinion – *An opinion on the merits of an investment decision made with the care, skill, prudence and diligence that a prudent person acting in a like capacity would use in the conduct of an enterprise of like character and aims.*
- Independent Fiduciary Recommendation – *An independent recommendation on an investment decision made solely in the interest of plan participants and their beneficiaries, regardless of who pays the independent fiduciary's fees.*

**Definitions developed by Investment Office Staff based on Legal concepts of Prudent Person Rule and ERISA Fiduciary Standards*